

**Statement of Alan W. Granwell,
Ivins, Phillips & Barker, on behalf of
Hitachi High Technologies America, Inc.**

My name is Alan Granwell, and I am a member of Ivins, Phillips & Barker, a Washington-based law firm specializing in U.S. federal taxation. Our firm has significant experience in dealing with all types of U.S. federal income tax issues involving foreign activities of U.S. taxpayers and the U.S. activities of foreign taxpayers. On behalf of our clients, we have been actively involved with the APA program since its inception, and I am grateful for the opportunity to discuss our views regarding the program with you today.

In your announcement of this hearing, you asked for comments regarding “the state of, and ideas for improving, timeliness and efficiency in handling APA matters,” “the accessibility of the APA program to taxpayers,” and “the effectiveness of the APA program generally,” among other issues. Today I would like to briefly address these three topics and to provide recommendations for your consideration.

Before I do so, I want to emphasize how important we believe the APA program is, not only for taxpayers, but also for the IRS itself. The APA program provides an essential mechanism for taxpayers and the IRS to achieve certainty with respect to transfer pricing issues in a cost-effective manner. Simply put, transfer pricing is fact-intensive. Resolving transfer pricing matters in an adversarial fashion requires great expenditures of time and money for all concerned and may lead to uncertain and unpredictable results. Mr. Snoke has spoken of the significance of these advantages from the viewpoint of the taxpayer. I would merely add that the

IRS itself can achieve savings: savings from the cost of adversarial proceedings and savings from the potential confusion of diffused decision making.

We have heard the APA program criticized as a special break for multinational corporations. We believe this criticism is fallacious and unfair in general. The truth is that the program provides significant benefits to the U.S. fisc. For instance, it was reported recently that the IRS has collected over \$800 million in rollback adjustments alone in connection with the program. We believe the IRS should be commended, not criticized, for thinking creatively about how to administer an increasingly complex tax system in an era of tightening budget constraints.

I turn now to your specific requests for comments.

First, we believe that the *efficiency* of the program could be improved by reducing the scope of inquiry in the case of renewal APAs to new issues presented by intervening changes in the taxpayer's businesses or structure. As an initial matter, we believe it is realistic for taxpayers to expect that a significant investment will be required with the first APA to educate the IRS participants about the details of a taxpayer's business. Once the taxpayer and the IRS have reached this first APA agreement, however, the taxpayer should not be required to "reinvent the wheel" in order to renew an APA.

Renewal agreements should not be seen as an opportunity for APA team members who may have been unhappy with certain aspects of the prior compromise to reopen settled issues in order to try for a "second bite of the apple." The perception among taxpayers that a renewal APA

does not provide a good investment return may explain in part the recently reported decline in the program's retention rate for taxpayers.

We also agree with comments made elsewhere that the efficiency of the APA process could be improved by increased employee retention in the program. A new team member may be just as capable as a departing team member. The new team member, however, must become familiar with the details of the taxpayer's business—as well as the parameters of his or her new job in many cases. This problem, moreover, feeds on itself: the longer an APA takes to complete, the more likely it becomes that one or more team members will depart, which in turn leads to further delays, increasing the chances of additional replacements. We have a suggestion in this regard. In our own view, program participants might be willing to pay higher user fees in order to have more assurance of a specific date for receiving an APA renewal determination. These increased user fees could be used, for example, to hire a more permanent staff with a required minimum tenure.

Second, we believe *accessibility* to the APA program could be improved by releasing additional guidance regarding the preferred U.S. negotiating position on certain routine, but substantive issues. The APA program has been in place now for 14 years, and a significant body of experience has developed over time. We believe it would enhance accessibility of the program to release formal guidance regarding issues that regularly arise in the negotiation of APAs. For example, taxpayers could benefit from IRS views regarding the appropriate methodology for selecting and screening comparables and the customary adjustments to their financial data in particular circumstances. The APA program has made available certain training materials

regarding these types of issues, but the materials are unclear and incomplete. More formalized guidance would give taxpayers a framework for their own submissions to the IRS and reduce the transaction costs of entering into the program.

We do not feel that redacted APAs or other taxpayer-specific releases would serve as an appropriate substitute for this type of guidance. The reality is that fewer—not more—taxpayers would participate in the APA program if the details of their internal pricing mechanisms were revealed to the public, even in shorthand or redacted form. An APA effectively substitutes for a transfer pricing audit in the field. The IRS is appropriately prohibited by law from disclosing taxpayer-specific information obtained through such audits. Similarly, the IRS is prohibited from disclosing taxpayer-specific information in a competent authority proceeding. It cannot be expected that the same type of information that would be collected in an audit or corollary competent authority negotiation would be made available publicly through the APA program. The release of redacted agreements is not a realistic alternative because the information must be redacted beyond usefulness in order to protect taxpayer-specific information. Increased accessibility to the APA program can be achieved by providing guidance as to routinely encountered issues, not taxpayer-specific data.

Third and finally, we believe that the *effectiveness* of the APA program can be increased by clarifying the role of IRS Examiners, Division Counsel, and other personnel from the Service Operating Divisions in the negotiation of APAs, particularly in bilateral APAs that do not involve rollbacks, litigation, or the examination of open years.

According to the Internal Revenue Manual, “[t]he Service should assign personnel to APA negotiations with a view to efficiency; therefore, IRS APA Teams should include the minimum number of people consistent with effective evaluation of the case, and with reasonable training needs of the Service.” Unfortunately, the Manual then proceeds to list eight categories of personnel from outside the APA program that can participate in the negotiations. In our experience, it is not unusual that more than “the minimum number of people” have been included in the APA negotiation process, and we believe that this expanded participation often impedes the successful and timely negotiation of an agreement. It makes the scheduling of meeting dates and telephone conferences and the negotiation of the agreement unduly cumbersome and, in certain unfortunate cases, adversarial. One explanation for this phenomenon, we believe, is that the exact role of Operating Division personnel in the APA negotiation process is not clearly defined.

Rev. Proc. 2004-40 provides that an APA has no effect on ongoing audits and also gives the Service Operating Divisions discretion with respect to rollback years. Otherwise, it provides only that “[t]he Service Operating Division field office responsible for the taxpayer's income tax return will be provided an opportunity to review and comment on the recommended U.S. competent authority negotiating position in the case of a bilateral or multilateral APA, and the proposed APA in the case of a unilateral APA.” The scope and breadth of this opportunity to review and comment is unclear, but it has been interpreted quite broadly, in our experience. In some cases, it has been interpreted to give IRS Examiners and Division Counsel the opportunity to attend every meeting and to oppose the taxpayer's very participation in the APA process—

even though the taxpayer is not under audit and rollback years are not involved. We consider this type of participation to be counter-productive.

As previously noted, taxpayers seeking a bilateral APA have little interest in winning concessions from the IRS because those concessions will simply inure to the benefit of the foreign taxing authority. Instead, taxpayers are motivated to persuade both the IRS and the foreign taxing authority to adopt negotiating positions to which the other jurisdiction will agree. In this regard, the most effective negotiating position typically is a principled position, based upon a neutral reading of U.S. and foreign tax law and a balanced understanding of the underlying economics. This position can be developed most effectively in a non-adversarial setting, consistent with the purpose of the APA program to resolve transfer pricing issues “in a principled and cooperative manner.”

We therefore believe that the effectiveness of the APA program can be enhanced by clarifying when and how IRS Examiners, Division Counsel, and other personnel from the Service Operating Divisions should participate in the negotiation of an APA. We further believe that there should be some variation in the scope of participation based upon whether the taxpayer and the APA Team anticipate that the APA will involve rollbacks, issues subject to litigation, or the examination of open years. Finally, in the context of a bilateral APA, we believe that further consideration should be given to the important checks and balances provided by the participation of the foreign taxing jurisdiction in the negotiation process.

In conclusion, we applaud the IRS for initiating and successfully maintaining the APA program. The program serves as a model for other forms of alternative dispute resolution, such as the Pre-Filing Agreement Program. A testament to its success has been the creation of similar programs by many of our trading partners, including Australia, Canada, China, France, Japan, Mexico, the Netherlands and the United Kingdom. These countries have followed the U.S. example because it assists taxpayers and taxing authorities achieve certainty with reduced costs.

For these reasons, we look forward to continued participation in the program.

We thank you for this opportunity to address issues of mutual concern.

I will be pleased to respond to any questions you may have.